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August 17, 2001

Cooking the Books: Social Security and Budget Gimmicks

Dear Democratic Colleague:

On Wednesday, the Bush Administration disclosed it is changing an accounting practice used during the entire history of Social Security. Over the past sixty-five years, whenever it was found that payroll tax credits to the Social Security trust funds had been understated in prior years, the general fund of the Treasury in the current year was debited and the trust funds credited by the amount of the understatement. Instead of charging the general fund this year for an underpayment of \$5.6 billion, the Bush Administration will go back and debit the general fund in those prior years when the payroll taxes were under-credited.

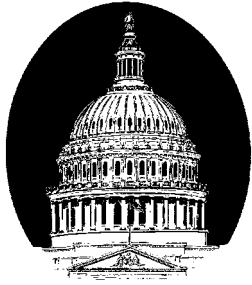
Why is the Bush Administration making this change, and why are they doing it in the middle of August? There's only one explanation. Next week, the Administration is releasing its new budget projections. The Bush Administration wants to obscure the fact that its tax cut wipes out the entire Medicare surplus — and probably taps the Social Security surplus, too.

We have been warning that the Bush tax cut invades Social Security and Medicare. We also warned it would deny resources for prescription drugs, defense and education. It looks like the new forecasts will bear out our warnings. Next Wednesday, when the White House releases its updated forecasts for 2001 and for 2001-2011, we will know whether President Bush is one gimmick away from tapping the Social Security surplus his first year in office.

An analysis prepared by the House Budget Committee's Democratic staff of the new Bush bookkeeping gimmick is attached. As soon as we receive the new OMB figures next week, we will be sending you a detailed analysis. On August 28, CBO will release its surplus estimates and we will provide you with a report about those as well. In the meantime, if you have any questions, feel free to call me or the Budget Committee's Democratic staff.

Sincerely,

John M. Spratt, Jr.
Ranking Democratic Member



HOUSE BUDGET COMMITTEE

Democratic Caucus

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August 17, 2001

Cooking the Books: Social Security and Budget Gimmicks

In its upcoming mid-session review, OMB reportedly will make two accounting changes that will have the net effect of increasing the amount of the non-Social Security surplus for FY 2001 by \$4.3 billion. A change to the accounting for Social Security payroll taxes will increase the non-Social Security surplus by \$5.6 billion. A second change, this one to the presentation of the Postal Service Fund, will reduce the non-Social Security surplus by \$1.3 billion. The net result is a \$4.3 billion increase in the non-Social Security surplus.

Accounting Change for Social Security

OMB reportedly will change the way it accounts for revisions to Social Security payroll tax receipts. The effect of this change will be to increase the amount of the non-Social Security surplus for FY 2001 by \$5.6 billion over what it would be if OMB followed the accounting practice that has been used for the last 65 years.

Under current law, the Treasury Department accurately records the *total* amount of federal revenues as they are received each fiscal year, but because it does not yet have complete data from employers on covered employment and wages, it divides total receipts between payroll taxes and income taxes based on estimates. Therefore, the Social Security Trust Fund is credited each quarter with an *estimate* of payroll taxes owed for that quarter, not the amount of payroll taxes actually paid for that quarter.

When it gets the employment and wage data about a year later, the Treasury Department is then able to make an accurate division of the prior year's tax receipts between (off-budget) payroll taxes and (on-budget) income taxes. Because the accurate split will differ slightly from the previous years' estimates, Treasury has to revise payroll and income taxes by offsetting amounts.

In recent years, the Administration has underestimated economic performance, which has meant that its projections of employee wage earnings were too low. Therefore, the amount of payroll taxes credited to the Trust Fund was also too low, and OMB has had to make adjustments to increase the amount of payroll taxes credited to the Trust Fund. This is the same kind of adjustment OMB will show in the upcoming mid-session review.

Up to now, OMB made all reconciling adjustments to the current year's receipts. Under this practice, the payroll taxes recorded for 2001 would equal the estimate of payroll taxes owed for 2001, plus any adjustments to previous years' estimates. The adjustments are in effect transfers from on-budget to off-budget (or vice versa); as part of any adjustment to payroll taxes, OMB would make an opposite adjustment to the amount of other government receipts for 2001. The opposite adjustment would keep total government receipts at the actual level recorded for the fiscal year.

Using this longstanding practice, OMB should *increase* (off-budget) Social Security payroll tax receipts by \$5.6 billion for 2001 and *reduce* other (on-budget) governmental receipts for 2001 by an equivalent \$5.6 billion. The effect of this change would be to reduce the non-Social Security surplus by \$5.6 billion and increase the Social Security surplus by \$5.6 billion, leaving the unified surplus unchanged.

Reportedly, OMB is scrapping this longstanding practice and instead will go back and adjust the level of payroll tax receipts for fiscal years already ended. Under this new method, OMB will make the above adjustments to payroll tax receipts for **FY 2000** and previous fiscal years by a total of \$5.6 billion. In that way, OMB will avoid the need to reduce the non-Social Security surplus in FY 2001 by that amount. OMB may show the on- and off-budget surpluses both ways (with and without the adjustment), and it will push for its new approach by arguing that the \$5.6 billion is unrelated to any action taken this year by the Congress or the Administration.

For several practical reasons, previous administrations have rejected this second accounting approach. It is difficult to revise historical tables; it is confusing for data users; there is the question of whether to credit back interest to the trust funds; and there may be problems with the statutory debt ceiling. In addition, these kinds of accounting changes are normally made only after consultation with CBO and the House and Senate Budget Committees. No such consultation occurred with regard to this accounting change. Finally, this new accounting practice is at variance with the way the federal government records other adjustments to totals for fiscal years already completed. For instance, re-estimates of credit subsidies for direct or guaranteed loans made in previous years are always recorded in the current fiscal year.

Change in Presentation for Postal Service Fund

Under current law, the receipts and disbursements of both the Social Security Trust Fund and the Postal Service Fund are considered "off-budget." Receipts and disbursements of the Postal Service Fund generally cancel each other out, but in any given year there is a relatively small surplus or deficit.

In general, calculations of the "available surplus" have started with the on-budget surplus and simply subtracted the surplus in the Medicare Trust Fund. Because it is off-budget along with the Social Security Trust Fund, the Postal Service Fund has also generally been excluded from calculations of the available surplus.

To isolate Social Security from the rest of the budget, OMB will in some of its presentations lump the Postal Service Fund in with the rest of the budget. Because the Postal Service Fund is expected to have a net deficit of \$1.3 billion for FY 2001, the "non-Social Security budget" will be lower by this amount.